Department of the Treasury	Internal Revenue Service	Office of Chief Counsel	**Notice**

CC-2009-027

August 21, 2009

Subject:	Frequently Asked Questions Regarding The Unified Partnership Audit And Litigation Procedures Set Forth In Sections 6221-6234	**Cancel Date**:	Effective until further notice

PURPOSE

This notice addresses frequently asked questions regarding the unified partnership audit and litigation procedures set forth in I.R.C. §§ 6221-6234 (the "TEFRA partnership procedures").

BACKGROUND

Although partnerships do not pay Federal income taxes they are required to file annual information returns reporting the partners' distributive shares of tax items. I.R.C. §§ 701 and 6031. The partners report their distributive shares of the tax items on their respective Federal income tax returns. I.R.C. §§ 701-704. To remove the substantial administrative burden occasioned by duplicative audits and litigation, and to provide consistent treatment of partnership tax items among partners in the same partnership, Congress enacted the unified partnership audit and litigation procedures as part of the Tax Equity and Fiscal Responsibility Act of 1982, Pub.L. No. 97-248, sec. 401, 96 Stat. 648. Petaluma FX Partners, LLC v. Commissioner, 131 T.C. No. 9, 2008 WL 4682543, *4 (2008).

Under the TEFRA partnership procedures, prior to assessing the tax liability of the partners, the Internal Revenue Service determines the tax treatment of partnership items in a partnership-level proceeding. I.R.C. §§ 6221 and 6225. Determinations at the partnership level are binding upon all direct and indirect partners of the partnership. Sente Inv. Club P'ship of Utah v. Commissioner, 95 T.C. 243, 247-250 (1990). In the absence of a partnership-level proceeding, the Service is bound by the partnership items as reported on the partnership return. Roberts v. Commissioner, 94 T.C. 853, 862 (1990).

Section 6231(a) provides that the TEFRA partnership procedures apply to any partnership except for partnerships with ten or fewer partners, all of which are: individuals who are not nonresident aliens; C corporations; or estates of deceased individuals. Thus, if any partner is a pass-thru entity, then the partnership is subject to the TEFRA partnership procedures regardless of the

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number of partners.[1] I.R.C. § 6231(a)(1)(B); Treas. Reg. § 301.6231(a)(1)-1(a)(2). The Service generally determines, based upon the partnership's information return, whether the TEFRA partnership procedures are applicable to the reported tax year.[2] I.R.C. §§ 6231(g) and 6233.

The Service must notify partners of when the audit of the partnership has begun (a notice of beginning of administrative proceeding or the "NBAP"), and of proposed adjustments to the partnership's information return, if any (a notice of final partnership administrative adjustment or the "FPAA"). I.R.C. § 6223. During the ninety-day period after the mailing of the notice of FPAA, the tax matters partner (the "TMP") may file a petition for judicial review. I.R.C. § 6226(a). If the TMP does not file a petition within that ninety-day period, any notice partner or any five percent group (section 6231(a)(11)) may, within sixty days after the close of the TMP's ninety-day period, file a petition for judicial review.[3] I.R.C. § 6226(b).

Partnership items flow through, appearing in the computation of the taxable income of the partners and affecting nonpartnership items on a partner's tax return. I.R.C. §§ 6230(a)(1) and 6231(a)(4)-(a)(6); Treas. Reg. § 301.6231(a)(5)-1; Petaluma FX Partners, LLC, 131 T.C. No. 9, 2008 WL 4682543, *5. There are two types of affected items: those that require only a computation of the tax immediately assessable; and those that require partner-level determinations made through a notice of deficiency. I.R.C. § 6230(a); Treas. Reg. § 301.6231(a)(6)-1; Petaluma FX Partners, LLC, 131 T.C. No. 9, 2008 WL 4682543, *4.

ANSWERS TO FREQUENTLY ASKED QUESTIONS

(A) Partnership Items

1. What is a partnership item?

A partnership item is any item required to be taken into account for the partnership's taxable year under any provision of Subtitle A of the Code, to the extent that regulations provide that it is more appropriately determined at the partnership level rather than at the partner level. I.R.C. § 6231(a)(3). These items include, but are not limited to: the partnership aggregate and each partner's share of items of income, gain, loss, deduction or credit of the partnership; the amount and type of any partnership liabilities; optional adjustments to the basis of partnership property pursuant to a section 754 election; and the amount of contributions to the partnership. Treas. Reg. § 301.6231(a)(3)-1. They also include the accounting practices, and the legal and factual determinations that underlie the determination of other partnership items. Treas. Reg. § 301.6231(a)(3)-1(b).

2. Should the Service determine a partner's outside basis at the partnership level?

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[1] Section 6231(a)(9) defines "pass-thru partner" to include trusts. Section 408(a) provides, for purposes of section 408, that the term "individual retirement account" (IRA) means a trust and that the bank is the trustee. Therefore, if an IRA is a partner in a partnership, the small partnership exception does not apply and the partnership will be subject to the TEFRA partnership procedures.

[2] No court has ruled on the application of the TEFRA partnership procedures to a partnership return providing there is only one partner that has elected out of the small partnership exception. Thus, the Service should follow both TEFRA and non-TEFRA partnership procedures, moving to dismiss any partnership-level litigation on the ground that the TEFRA partnership procedures do not apply because the contents of the return demonstrate that it is not a "partnership return" under section 6233.

[3] The total time period in which a partner may petition the FPAA may be more than one hundred fifty days due to weekends and holidays. See I.R.C. § 7503 (time for performance of acts where last day falls on Saturday, Sunday or legal holiday).

Outside basis, which is a partner's basis in the partner's partnership interest, is relevant when: a partnership distributes to a partner that partner's share of the partnership's loss; the partnership distributes cash or property to a partner; or a partner sells that partner's partnership interest. I.R.C. §§ 704(d), 731, 732, 741 and 1001.

Most, but not all, of the component items of outside basis are partnership items, including: the basis of contributions to the partnership; distributions from the partnership; the partner's share of nontaxable income, taxable income, losses and deductions; and the partner's share of partnership liabilities. I.R.C. § 705; Treas. Reg. § 301.6231(a)(3)-1; Nussdorf v. Commissioner, 129 T.C. 30, 42-44 (2007).

Partner-level determinations include, in the absence of a section 754 election by the partnership, the cost to purchase the partnership interest or the transferor's basis in the partnership at the time of acquisition by gift, bequest, transfer or exchange. Dial USA, Ltd. v. Commissioner, 95 T.C. 1, 4 (1990). See Petaluma FX Partners, LLC , 131 T.C. No. 9, 2008 WL 4682543, *10; IRM 8.19.1.6.9.4(f), *Issues With Both Partnership and Partner Level Elements*.

If, however, the Service determines, at the partnership level, that the partnership was a sham, (*i.e.*, that no partnership exists), then that determination includes a determination that outside basis, for each partner, for that taxable year, was zero.[4] Petaluma FX Partners, LLC, 131 T.C. No. 9, 2008 WL 4682543, *9-*11. There would be no partner-level factual determinations left to be made to calculate outside basis because, as a matter of law, there can be no basis in a nonexistent partnership. Id.

3. Should the Service determine at the partnership level that, under section 465, the partner's distributive share of losses exceeds the partner's amount at risk?

Regarding section 465, the Service must make determinations at both the partnership level and at the partner level. See IRM 8.19.1.6.9.4(2)(d), *Issues With Both Partnership and Partner Level Elements*. Partnership-level items include the partners' shares of partnership liabilities and the character of the liabilities as recourse or nonrecourse. See Id. Partner-level items include any arrangements with third parties insulating the partner from loss, and whether a partner is a related party under section 465(b)(3). See Id.; Hambrose Leasing 1984-5 Ltd. P'ship v. Commissioner, 99 T.C. 298, 308-309 (1992) (whether partners protected against loss is a partner-level issue); Roberts v. Commissioner, 94 T.C. 853, 861-863 (1990) ("The existence and effect of the side agreements at issue are not items that a TEFRA partnership must account for under subtitle A in their books, records, or returns.").

4. Is the section 1446 withholding tax a partnership item?

Yes. Section 1446 is a provision of Subtitle A more appropriately determined at the partnership

[4] The determination that a partnership was not a partnership for a taxable year is a partnership-level determination that must be included in the "Remarks" section of the FPAA incorporating by reference the attached "Explanation of Adjustments". Petaluma FX Partners, LLC v. Commissioner, 131 T.C. No. 9, 2008 WL 4682543, *6 (2008). See Treas. Reg. § 301.6233-1 ("Any final partnership administrative adjustment or judicial determination resulting from a proceeding under subchapter C with respect to such taxable year may include a determination that the entity is not a partnership for such taxable year as well as determinations with respect to all items of the entity that would be partnership items, as defined in I.R.C. § 6231(a)(3) and the regulations thereunder, if such entity had been a partnership in such taxable Year . . . .").

level than at the partner level. Thus, examinations with respect to section 1446 are subject to the TEFRA partnership procedures. I.R.C. § 6231(a)(3); Treas. Reg. § 301.6231(a)(3)-1(a)(1)(v).

5. How does the Service determine, for purposes of section 165(c), the profit motive of the partnership?

For purposes of section 165(c), the Service determines the profit motive of the partnership by reference to the state of mind of the general partner(s) acting on the partnership's behalf. See Brannen v. Commissioner, 722 F.2d. 695, 705 n.10 (11th Cir. 1984) ("[T]he tax court properly looked to the general partner's actions in determining whether the partnership, as an entity, was operated in a business-like manner."); Garcia v. Commissioner, 96 T.C. 792, 797 (1991).

(B) Notices

1. Who is entitled to notice of partnership-level audit proceedings?

The Service must mail the NBAP and the notice of FPAA to: the TMP; all notice partners; and the designated representative of any section 6223(b)(2) notice group. I.R.C. §§ 6223(a), (b). Failure to issue the requisite notice triggers either conversion of the partner's partnership items to nonpartnership items or the availability of an election to do so. I.R.C. § 6223(e). See Wind Energy v. Commissioner, 94 T.C. 787, 789-794 (1990).

2. Is the partnership entity a party to partnership-level audit and litigation proceedings?

No. The partnership entity is not a party to the partnership-level audit or litigation proceeding. Chef's Choice Produce, Ltd. v. Commissioner, 95 T.C. 388, 395 (1990). The partners whose tax liabilities will be affected by the outcome of a partnership-level proceeding are the parties in interest in any partnership-level audit or litigation proceeding. Id. The dissolution or termination of the partnership entity does not affect the partnership-level proceedings. Id.

3. How do the partners designate a TMP?

The designation of a TMP for a specific taxable year is made or terminated only as provided in Treas. Reg. § 301.6231(a)(7)-1. I.R.C. § 6231(a)(7). A court appointing a new TMP for litigation purposes is not subject to that regulation. See Tax Court Rule 250.

4. To what addresses should the Service mail notices?

The Service may use the names, addresses and profits interests shown on: the partnership return; any written statement filed by any person with the Service at least thirty days before the Service mails the notice to the TMP; and any updates by the Service itself, (*e.g.*, the partner's last known address). I.R.C. §§ 6223(c)(1) and (c)(2); Treas. Reg. § 301.6223(c)-1. The Service should, for protective purposes, send duplicate copies of the notice to any conflicting addresses.

The Service should mail generic notices to "THE TAX MATTERS PARTNER" at the address of the partnership. I.R.C. § 6223(a); Treas. Reg. § 301.6223(a)-1. The Service should also mail the notices to the designated TMP at the TMP's address.

5. Which partners are notice partners?

If the partner has a one percent, or more, interest in the profits of the partnership, or if the

partnership has one hundred or fewer partners, then the partner is a notice partner entitled to the NBAP and the notice of FPAA. I.R.C. § 6223(b)(1).

6. May multiple partnership years be included in the same NBAP and FPAA?

If all partners remain the same over multiple tax years, then the Service may address those multiple tax years in a single NBAP and a single FPAA. I.R.C. §§ 6223, 6103(h)(4).

7. What is a notice group?

Section 6223(b)(2) provides that, upon request, the Service must mail the NBAP and the notice of FPAA to the designated member of a group of partners that, in the aggregate, has a five percent or greater interest in the profits of the partnership. A section 6223(b)(2) notice group is distinct from a section 6231(a)(11) "five percent group," which, under section 6226(b)(1), may petition for judicial review of an FPAA. See PCMG Trading Partners XX, L.P. v. Commissioner, 131 T.C. No. 14, 2008 WL 5191382, *4 (2008) (five percent group petition).

8. How do failures of the TMP affect TEFRA partnership audit and litigation proceedings?

The failure of the TMP, a pass-thru partner, the representative of a notice group or any other representative of a partner to perform any act required by the TEFRA partnership procedures does not affect the applicability of any TEFRA partnership proceeding or adjustment. I.R.C. § 6230(f).

9. Must the FPAA include an explanation of adjustments made therein?

Yes. The FPAA must include a sufficient explanation of the grounds for adjustment to avoid the burden of proof shifting to the Service. I.R.C. § 7522; Shea v. Commissioner, 112 T.C. 183, 197 (1999). The "Remarks" section of the FPAA should provide the explanation or incorporate by reference a separate document entitled "Explanation of Adjustments." The Service should send the same FPAA to all partners entitled to notice. See I.R.C. § 6223(a).

The Service may issue an FPAA that determines that partnership items, as reported on the partnership return, are correct. Harbor Cove Marina Partners P'Ship v. Commissioner, 123 T.C. 64, 78 (2004). Partners may petition a "no change" FPAA. For example, partners may seek additional deductions.

10. What is the limitations period for issuing an FPAA?

There is no statute of limitations for issuing an FPAA. The Service may adjust partnership items arising in a year for which all periods of assessment have expired as long as the adjustments affect a partner year (*e.g.*, an NOL carryforward) for which the assessment period has not expired. I.R.C. §§ 6226(c) and (d)(1)(A); Kligfeld Holdings v. Commissioner, 128 T.C. 192, 202-207 (2007). Cf. Bob Hamric Chevrolet, Inc. v. United States, 849 F.Supp. 500, 512 (W.D. Tex. 1994) ("When a partnership loss, deduction or credit allocated to a partner in one year carries over or back to other taxable years at the partner level, such carryover or carry back is an affected item."). See Bahar v. United States, No. 08 Civ. 4738 (WHP), 2009 WL 1285946, *4 (S.D.N.Y. May 4, 2009).

11. If a subsidiary corporation is a partner in a TEFRA partnership, what is the effect of the bankruptcy of the parent corporation?

If a partner is a subsidiary corporation, then the parent corporation will generally be a partner pursuant to section 6231(a)(2)(B). See Rev. Rul. 2006-11. Upon the filing of a petition in Bankruptcy Court naming the parent corporation as a debtor, the Service will treat as nonpartnership items the parent corporation's partnership items; however, the Service will continue to treat as partnership items the partnership items of the subsidiary corporation and other nonbankrupt subsidiary corporations in the consolidated filing group. I.R.C. § 6231(c); Treas. Reg. § 301. 6231(c)-7. See Treas. Reg. § 301.6231(a)(2)-1(a)(4)(iii); IRM 4.31.7.6.4.1, *Parent/Subsidiary*.

(C) Petitions

1. Who is considered a party to a section 6226 action?

A partner, not the partnership entity, files a petition for readjustment of partnership items. I.R.C. § 6226. Thus, the petitioner is the partner, not the partnership. Chef's Choice Produce, Ltd., 95 T.C. at 395-396; Barbados #6 Ltd. v. Commissioner, 85 T.C. 900, n.1 (1985). Court filings in TEFRA partnership cases should never refer to the partnership as "the petitioner" or refer to "the petitioning partnership". The partnership name in the caption reflects the aggregate nature of the proceedings, not that the partnership is the petitioner.[5] See Tax Court Rules 240(d) and 247.

The Service and the Tax Court will treat each partner with an interest in the outcome of the petition as a party to the action. I.R.C. § 6226(c); Tax Court Rule 247. Partners include any individual or entity whose income tax liability under Subtitle A of the Code is determined, in whole or in part, by taking into account, directly or indirectly, partnership items of the partnership. I.R.C. § 6231(a)(2).

For purposes of discovery, the Tax Court regards nonparticipating partners as third parties. See Tax Court Rule 75(b) (third-party deposition of a partner).

2. What is a participating partner?

Participating partners include the partner that filed the petition and partners that have filed, in accordance with Tax Court Rule 245, a notice of election to intervene or a notice of election to participate. Tax Court Rule 247(b).

Whenever Tax Court Rules require that the Service file a paper with the Tax Court, the Service must serve copies of that paper upon all participating partners and the TMP. Tax Court Rule 246(c).

3. Should the Service identify partners at the partnership-level?

Yes. The identification of the partners is a partnership item. Katz v. Commissioner, 335 F.3d 1121, 1128-1129 (10th Cir. 2003); Blonien v. Commissioner, 118 T.C. 541, 551-552 (2002).

But see Grigoraci v. Commissioner, T.C. Memo. 2002-202, 2002 WL 1835711, *5-*7 ("Under the circumstances of this case, we hold that a determination that the partners of record were not the true and actual partners is not a 'partnership item' . . . ."); Hang v. Commissioner, 95 T.C. 74, 82 (1990) ("[T]he determination of whether income should be reallocated from a shareholder of record to someone who is not a shareholder of record is more appropriately determined at the

[5] Section 6226 and Tax Court Rules 240 through 251 contemplate only a single petitioner.

shareholder level."); Alpha I, L.P. ex rel. Sands v. United States, 86 Fed.Cl. 126, 134 (2009).

In light of this uncertainty, the Service should determine the identities of partners at the partnership level because, even if the court determines the issue must be resolved at the partner level, section 6229(d) will likely suspend the statute of limitations. Duplicative protective nonpartnership procedures may be necessary in some circumstances.

4. May the petitioner, or petitioner's counsel, prevent contact with other partners?

No. For purposes of contact, the petitioner (even if the TMP) does not represent the other partners, and petitioner's counsel represents only those on behalf of whom an entry of appearance is made. See I.R.C. § 6224(a) ("Any partner has the right to participate in any administrative proceeding relating to the determination of partnership items at the partnership level."); Tax Court Rule 75 (third-party deposition of a partner).

5. Should the Service move to dismiss a petition filed during the section 6226(a) ninety-day period by someone other than the TMP?

If any person other than the valid TMP files a petition during the section 6226(a) ninety-day period, then the Service should determine whether there is a valid TMP willing to ratify the petition by filing an amended petition in the name of the proper party. If ratification is unavailable, then the Service should prepare either a Tax Court Rule 250 motion to appoint a TMP to ratify the petition, or a motion to dismiss the action for lack of jurisdiction under section 6226(a). See Montana Sapphire Assoc., Ltd. v. Commissioner, 95 T.C. 477, 483 (1990) ("We do not believe that it is appropriate to dismiss the petition under these circumstances without first giving (1) the partnership the opportunity to advise the Court of the name of a person to be appointed TMP and (2) the TMP the opportunity of ratifying the original petition."); CCDM 35.3.7.2(5), *Jurisdictional Motions*. If the petitioner is a notice partner or a section 6231(a)(11) five percent group, then the court may treat the petition as filed on the last day of the section 6226(b) sixty-day petition period. I.R.C. § 6226(b)(5).

Courts have upheld section 6226(a) TMP petitions despite the failure to comply with the regulations regarding designation of the TMP. See Mishawaka Prop. Co. v. Commissioner, 100 T.C. 353, 367 (1993) ("Whether we imply ratification by the partner who was qualified to be the TMP or by a majority of the partners who could have designated a TMP, the result would be the same."); Chomp v. Commissioner, 91 T.C. 1069, 1078 (1988) ("As stated above, the question is whether Pearl was duly authorized to file the petition in this case, not whether he properly notified respondent.").

6. Should the Service move to dismiss a petition filed during the section 6226(b) sixty-day period by someone other than a notice partner or a five-percent group?

If the section 6226(b) petitioner is not a notice partner or a section 6231(a)(11) five-percent group, then the Service should seek ratification by any notice partner or five-percent group before filing a motion to dismiss for lack of jurisdiction under section 6226(b). See CCDM 35.3.7.2(5), *Jurisdictional Motions*. But see Gov't Arbitrage Trading Co. v. Commissioner, T.C. Memo. 1994-136, 1994 WL 102638, *3 (denying opportunity to obtain ratification).

7. Why does the caption identify as TMP the petitioner who filed during the section 6226(b) sixty-day period?

Tax Court Rule 240(d) requires that, if the petitioning partner is the TMP, then the caption should identify the petitioning partner as such regardless of when the petition was filed.

8. Do the FPAA and the Answer limit the court's jurisdiction in a section 6226 action?

No. Section 6226(f) provides that, regardless of whether the Service raised adjustments in the FPAA, the Answer or in any other manner, the court has jurisdiction to determine: all partnership items of the partnership for the partnership taxable year to which the notice of FPAA relates; the proper allocation of the partnership items among the partners; and the applicability of any penalty, addition to tax or additional amount that relates to an adjustment to a partnership item. The purpose of the Answer in a section 6226 action is to place the court and the parties on notice of disputes. See PAA Mgmt., Ltd. v. Commissioner, 962 F.2d 212, 218 (2nd Cir. 1992).

9. Does the court, in a partnership-level proceeding, have jurisdiction to abate interest under section 6404?

No. In a partnership-level proceeding, the court's jurisdiction does not extend to abatement of interest under section 6404. See I.R.C. §§ 6226(f) and 6231(a)(3); Treas. Reg. § 301.6231(a)(3)-1; Alpha I, L.P. ex rel. Sands v. United States, 86 Fed. Cl. 126, 134 (2009) ("[T]he language of 26 U.S.C. § 6226(f), providing for jurisdiction over any 'additional amount which relates to an adjustment to a partnership item,' 26 U.S.C. § 6226(f), refers solely to the application of penalties, [citations omitted]."); Affiliated Equip. Leasing II v. Commissioner, 97 T.C. 575, 577-578 (1991) ("[S]ection 6621(c) interest is not a 'partnership item' and is not within the Court's scope of review in a partnership level proceeding.").

(D) Assessment

1. When may the Service assess penalties?

For partnership taxable years ending after August 5, 1997, the Service determines at the partnership level the applicability of any penalty, addition to tax or additional amount that relates to an adjustment to a partnership item. I.R.C. § 6221. The Service and the court consider partnership-level defenses by reference to the actions and state of mind of the managing partner. Stobie Creek Inv., LLC v. United States, 82 Fed.Cl. 636, 703 (2008). See Klamath Strategic Inv. Fund ex rel. St. Croix Ventures v. United States, No. 07-40861, 2009 WL 1353118, * 8 (5th Cir. May 15, 2009); Tigers Eye Trading, LLC v. Commissioner, T.C. Memo. 2009-121, 2009 WL 1475159, *10 (2009). But see Clearmeadow Investments, LLC v. United States, No. 05-1223 T, 2009 WL 1784247, *7-*9 (Ct. Cl. June 17, 2009) (court lacks jurisdiction at partnership level to consider applicability of reasonable cause exception to the section 6664(c) gross valuation misstatement penalty). The Tax Court has held that the Service may assess penalties that relate to partnership items, without issuing a notice of deficiency, even if the underlying deficiency or the penalty itself requires partner-level determinations. Domulewicz v. Commissioner, 129 T.C. 11, 23 (2007), *appeal docketed*, No. 08-1676 (6th Cir. May 20, 2008). See also section 6230(a)(2); Treas. Reg. § 301.6231(a)(6)-1(a)(3); Tigers Eye Trading, LLC, T.C. Memo. 2009-121, 2009 WL 1475159, *24. Partners may raise partner-level defenses to a penalty (those that are personal to the partner, or that are dependent on the partner's separate return) only through a refund action. Treas. Reg. § 301.6221-1(d); I.R.C. § 6230(c)(4); Tigers Eye Trading, LLC, T.C. Memo. 2009-121, 2009 WL 1475159, *10. If the penalties relate to affected items, then protective duplicative assessment procedures may be required. See Chief Counsel Notice 2009-011, *Protective Assessments of Affected Items in TEFRA Partnership Cases*.

2. How does a partner challenge an assessment?

If the Service has assessed a computational adjustment without a notice of deficiency, then a partner may challenge the assessment only after making payment. I.R.C. §§ 6230(a), (c) and (d); I.R.C. § 6511(g). If the Service determines that it made an error in the computation, and if the taxpayer has not yet paid the tax liability, the Service may abate the assessment, in whole or in part, under section 6404. See I.R.C. § 6404.

If the Service has issued a statutory notice of deficiency, then, under section 6213(a), the partner has ninety days to petition the deficiency in Tax Court. Otherwise, the partner can pay the deficiency and seek a refund under section 7422.

3. What is the notice of computational adjustment?

For purposes of section 6230(c)(2), the Service is deemed to have sent to the partner a "notice of computational adjustment" when it sends to the partner Form 4549, *Income Tax Examination Changes*, showing the adjustments making the partner's tax return consistent with partnership-level determinations and the subsequent change to tax liability. See IRM 8.19.1.6.9.7(3), *Computational Adjustments.*

4. When may the Service issue an affected item notice of deficiency?

The Service should not issue an affected item notice of deficiency before the conclusion of a partnership-level proceeding regarding partnership items that affect the items in the notice of deficiency. GAF v. Commissioner, 114 T.C. 519, 524-528 (2000).

5. What is a Munro stipulation?

In Munro v. Commissioner, 92 T.C. 71 (1989), the Tax Court held that, in determining whether a deficiency attributable to nonpartnership items exists, the Service must ignore partnership items that are included on a taxpayer's return and subject to a separate and ongoing TEFRA partnership proceeding. The Munro stipulation is an agreement between the Service and a taxpayer providing: that, for purposes of computing the deficiency, the Service has treated the taxpayer's partnership items, which are subject to an ongoing TEFRA partnership proceeding, as if correctly reported on the taxpayer's return; and the Service can assess, at the conclusion of a TEFRA partnership-level proceeding, any change to the non-TEFRA deficiency liability caused by resolution of that TEFRA partnership-level proceeding (*e.g.*, a change to the non-TEFRA deficiency liability attributable to an increased tax bracket). In the absence of the stipulation, in accordance with Munro, the Service would have to include the tax bracket increase as part of the non-TEFRA deficiency. For oversheltered returns, section 6234 supersedes the Munro procedures. See CCDM 35.2.1.1.16, *TEFRA: Munro Stipulation for Deficiency Cases*.

6. May the Service, without issuing an FPAA, adjust partnership and affected items on a partner's tax return?

Yes. If a partner fails to report the partner's share of partnership items in the same manner as reported on the partnership return, and if that partner fails to notify the Service of the inconsistency, then the Service may assess the difference without issuing an FPAA. I.R.C. § 6222(c). A notice of deficiency is necessary only if a partner-level determination is required. I.R.C. § 6230(a)(2).

(E) Statute of Limitations

1. What is the relationship between section 6501 and section 6229?

Section 6501(a) provides the period of limitations within which the Service may assess any tax imposed by Title 26 of the United States Code, including tax attributable to partnership and affected items. Section 6229(a) provides that each partner's section 6501 assessment period for tax attributable to partnership and affected items will not expire before the date that is three years after the later of: the date on which the partnership return for the taxable year was filed or the last day for filing the return for that year (determined without regard to extensions). Thus, section 6501 may provide a longer period of limitations than the minimum period for assessment under section 6229. Rhone-Poulenc Surfactants & Specialties, L.P. v. Commissioner, 114 T.C. 533, 542-543 (2000). See also Curr-Spec Partners, L.P. v. Commissioner, No. 08-60815, 2009 WL 2437764, *3 (5th Cir. 2009); AD Global Fund, LLC v. United States, 481 F.3d 1351, 1354-1355 (Fed. Cir. 2007); Andantech L.L.C. v. Commissioner, 331 F.3d 972, 976-977 (D.C. Cir. 2003).

2. If a TMP is an entity, who signs the consent to extend the period for assessing tax attributable to partnership and affected items?

A TMP may extend the period for assessing tax attributable to partnership and affected items with respect to all partners. I.R.C. § 6229(b)(1)(B). If a TMP is a partnership or a limited liability company, the Service must determine who has authority under State law to sign for the TMP entity. See IRM 4.31.2.6.4(2), *Persons Empowered to Sign A Consent*.

Consider, for example, partnership X. For tax year A, partnership X has designated as its TMP Y LLC. Z corporation is Y LLC's sole member-manager and, under State law, has authority to bind Y LLC. John is Z's chief financial officer and, under State law, has authority to bind Z corporation. John should sign the consent to extend the limitations period for tax year A for partnership X as follows: Y LLC, Tax Matters Partner of X, by Z Corporation, Manager of Y LLC, by John, CFO.

For tax years beginning before June 28, 2002, if a subsidiary in a consolidated filing group is the TMP of a partnership, then the Service should obtain the signature of an officer of the subsidiary and, for protective purposes, an officer of the parent. See Treas. Reg. § 1.1502-77A(a) and (e) for rules to identify the proper corporation to sign the statute extension as the parent corporation. For tax years beginning on or after June 28, 2002, if a subsidiary in a consolidated filing group is the TMP of a partnership, then the signature of only the TMP subsidiary is required on any statute extension signed by the TMP on behalf of the partners of the partnership. See Treas. Reg. § 1.1502-77(a)(3)(v); IRM 4.31.2.6.4(3) and (4), *Persons Empowered to Sign A Consent*.

3. May partners secretly replace the TMP before the TMP signs the consent to extend the assessment period for tax attributable to partnership and affected items?

No. If the Service does not know, and has no reason to know, of the designation of a new TMP, the partners are estopped from arguing that the properly designated former TMP lacked authority to sign a consent form. The Service must be able to rely on the acts of a properly designated TMP. San Gabriel Energy v. Commissioner, T.C. Memo. 1994-150, 1994 WL 122102, *4-*5 (1994).

4. May anyone other than the TMP sign a consent to extend the period for assessing tax attributable to partnership and affected items?

Yes. If the partnership has authorized, in writing, a person other than the TMP to enter into an agreement, such as a consent to extend the limitations period, that person also may extend the partnership or affected item assessment period with respect to all partners. I.R.C. § 6229(b)(1)(B). The partnership may authorize a person other than the TMP by filing with the Service, under Treas. Reg. § 301.6229(b)-1, a statement signed by all persons who were general partners (or, in the case of an LLC, member-managers) at any time during the year or years for which the authorization is effective.

If it is too late to obtain a new consent, the Service should consider whether the partnership agreement serves as a written authorization for the person who has already signed a consent. Cambridge Research and Dev. Group v. Commissioner, 97 T.C. 287, 301-302 (1991).

The TMP's power of attorney, pursuant to Form 2848, may sign an extension on behalf of the TMP. The preference, however, is to have the TMP personally sign significant documents. See IRM 4.31.2.2.5,(1)(b), *Power of Attorney Appointed by the Tax Matters Partner*.

If the valid designation of a TMP is uncertain, then the Service should, for protective purposes, obtain from each partner a consent to extend the assessment period for tax attributable to partnership and affected items using Form 872-I or successor forms. Form 872-I expressly refers to partnerships and affected items as required by section 6229(b)(3). See Ginsburg v. Commissioner, 127 T.C. 75, 89 (2006).

For tax years beginning before June 28, 2002, the Service should obtain the signature of an officer of the parent corporation regardless of whether the subsidiary or the parent is the partner. For tax years beginning on or after June 28, 2002: if the partner is a common parent of a consolidated group, the Service should obtain the signature of an officer of the parent corporation; but, if the partner is a subsidiary corporation, both the subsidiary and the parent of the consolidated group should sign the consent to extend the assessment period. See Treas. Reg. §§ 1.1502-77(a)(2)(iv) and (a)(6)(iii) (for tax years beginning on or after June 28, 2002); Treas. Reg. §§ 1.502-77A(a) and (e) (for tax years beginning before June 28, 2002); IRM 4.31.2.6.3(3)(c) and (d), *Extension of Investor Statute for TEFRA and Non-TEFRA Items*; IRM 25.6.22.6.2.1(6)(l), *Subsidiary of Consolidated Group as a Partner in a TEFRA Partnership (Forms 872-I and 872-IA)*.

5. Does fraud affect the assessment period for tax attributable to partnership and affected items?

Yes. If any partner has, with intent to evade tax, signed or participated in the preparation of a partnership return that includes a false or fraudulent item, then: regarding the signing or participating partners, the Service may assess at any time any tax imposed by Subtitle A of the Code that is attributable to any partnership or affected item for the partnership taxable year to which the return relates; and regarding all other partners, the section 6229(a) assessment period is extended from three years to six years. I.R.C. § 6229(c)(1). Compare I.R.C. § 6229(c)(1) with I.R.C. § 6501(c)(1) ("In the case of a false or fraudulent return with the intent to evade tax, the tax may be assessed . . . at any time.").

6. Does a partnership's omission from gross income affect the assessment period for tax attributable to partnership and affected items?

Yes. If any partnership omits from gross income more than twenty five percent of the amount of

gross income stated on its return, then the section 6229(a) assessment period is extended from three years to six years for all partners. I.R.C. §§ 6229(c)(2). Both the definition of gross income and the adequate disclosure provision of section 6501(e)(1)(a) are encompassed in section 6229(c)(2). Rhone-Poulenc Surfactants & Specialties, 114 T.C. at 540-551; CC & F Western Ltd. Partnership v. Commissioner, T.C. Memo. 2000-286, 2000 WL 1276708, at *3, aff'd, 273 F.3d 402 (1st Cir. 2001).

The Ninth Circuit in Bakersfield Energy Partners, L.P. v. Commissioner, No. 07-74275, 2009 WL 16776896, (9th Cir. June 17, 2009), held that it was bound by Colony, Inc v. Commissioner, 357 U.S. 28, 33 (1958), and thus, an overstatement of basis cannot constitute an omission from gross income for purposes of the six-year period of limitations. On July 30, 2009, the Federal Circuit similarly held in Salman Ranch, Ltd v. United States, No. 2008-5053, reversing and remanding 79 Fed. Cl. 189, 193-200, that section 6501(e)(1)(A) is not applicable to an alleged overstatement of basis. But see Home Concrete & Supply, LLC v. United States, 599 F.Supp.2d 678, 690 (E.D.N.C. 2008) (overstatement of basis can constitute an omission from gross income for purposes of the six-year period of limitations); Brandon Ridge Partners v. United States, No. 8:06-cv-1340-T-24MAP, 100 A.F.T.R.2d 2007-5347, *2007-5351-*2007-5353 (M.D.Fla. 2007) (same). All cases with this issue must be coordinated with the Office of the Associate Chief Counsel (Procedure and Administration).

7. Does a partnership's failure to file a return affect the assessment period for tax attributable to partnership and affected items?

Yes. If a partnership fails to file a return for a tax year, the Service may assess at any time any tax attributable to a partnership or affected item arising in that year. I.R.C. § 6229(c)(3). For this purpose, a section 6020(b) substitute return is not a partnership return. I.R.C. § 6229(c)(4).

8. Does the mailing of an FPAA affect the assessment period for tax attributable to partnership and affected items?

Yes. The mailing of an FPAA to the TMP suspends the assessment period for tax attributable to partnership or affected items: for the period in which a partner may file a petition for readjustment and for one year thereafter; and if a partner files a petition, until the decision of the court is final and for one year thereafter. I.R.C. § 6229(d).

Section 7481 provides the date upon which a Tax Court decision is final. Quick v. Commissioner, 110 T.C. 172, 182 (1998). For purposes of section 6229(d), the principles of section 7481(a) also determine the date on which a decision of a United States district court or the Court of Federal Claims is final. I.R.C. § 6230(g). Thus, the appeal period (ninety days in Tax Court and sixty days in district court and the Court of Federal Claims) affects the computation of the date the decision becomes final. I.R.C. § 7483; FED. R. APP. P. 4(a)(1)(B) and 13(a)(1).

9. Does the partnership's failure to identify a partner affect the assessment period for tax attributable to partnership and affected items?

Yes. If the partnership return does not provide the name, address and taxpayer identification number of a partner, and if either the Service has mailed the FPAA before the expiration of the section 6229(a) assessment period or the partner has failed to comply with section 6222(b), then, regarding that partner, the assessment period for any tax imposed by Subtitle A of the Code that is attributable to any partnership or affected item for the partnership taxable year of the partnership return will not expire before the date that is one year after the date upon which the

name, address and taxpayer identification number of the partner are furnished to the Service pursuant to Treas. Reg. § 301.6223(c)-1. I.R.C. § 6229(e); Treas. Reg. § 301.6229(e)-1.

(F) Settlement

1. May the Service settle disputes regarding partnership items with partners?

Yes. Section 6224(c)(1) allows a partner to enter into a settlement agreement determining with finality the correct treatment of partnership items for a partnership taxable year. Section 6224(c)(2) provides other partners the right to request settlement terms for the partnership taxable year that are consistent with the previously executed settlement agreement.

The partnership items of a partner for a partnership taxable year become nonpartnership items as of the date the partner and the Service, or the Department of Justice, enter into a settlement agreement with respect to partnership items. I.R.C. § 6231(b)(1)(C). Settlement agreements that convert partnership items of a partner for a partnership taxable year into nonpartnership items include: Form 870-P, *Settlement Agreement for Partnership Adjustments*; Form 870-PT, *Settlement Agreement for Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax and Additional Amounts*;[6] Form 870-L, *Settlement Agreement for Partnership Adjustments and Affected Items*; Form 870-LT, *Settlement Agreement for Partnership Items and Partnership Level Determinations as to Penalties, Additions to Tax and Additional Amounts, and Agreement for Affected Items*; Form 906, *Closing Agreement on Final Determination Covering Specific Matters*;[7] and correspondence between a partner and the Department of Justice that includes an offer and acceptance of a settlement agreement resolving all disputed partnership items. Neither the entry of a court decision, nor a stipulation of settled issues, converts the partnership items of a partner for a partnership taxable year into nonpartnership items. I.R.C. § 6231(b).

If the settlement agreement does not leave any partnership items in dispute, then the period for assessing the agreed items shall not expire before one year after the date of the conversion of the partnership items into nonpartnership items under section 6231(b)(1)(C). I.R.C. § 6229(f). A partner may consent to extend the assessment period for tax attributable to the converted items or items affected thereby; however, neither the TMP, nor any person authorized by the partnership in writing to enter into an extension agreement, may consent, with respect to all partners, to extend the section 6229(f) minimum assessment period. See I.R.C. § 6229(b); IRM 4.31.2.6.6(1), *Items Becoming Nonpartnership Items.* Furthermore, a partner for whom a settlement agreement has converted that partner's partnership items into nonpartnership items will no longer be a party to a section 6226 action regarding those partnership items and will no longer be bound by any court decision therein. I.R.C. § 6226(d)(1)(A); Tax Court Rule 247(a).

2. If a partner enters into a settlement agreement with the Department of Justice, must that partner settle separately with the Service?

The United States Attorney General has authority to settle cases referred to the Department of Justice. I.R.C. § 7122(a). Thus, if a partner enters into a settlement agreement with the

[6] The Form 870-PT does not resolve partner-level defenses to penalties determined at the partnership level. Thus, the taxpayer may file a refund claim to raise partner-level defenses to those penalties under section 6230(c). See Treas. Reg. § 301.6221-1(d).
[7] Delegation Order 4-19 identifies who, from the Service, may sign these forms.

Department of Justice, a separate settlement with the Service is not necessary to the extent that it is limited to the years and matters that were referred to DOJ. In contrast, if the settlement covers other years or matters that were not referred to DOJ, then a separate settlement with the Service is required because DOJ does not have authority to settle those years or matters. As a practical matter, however, even when DOJ has settlement authority, DOJ normally coordinates settlements with the Office of Chief Counsel.

3. How does a settlement agreement with a pass-thru partner affect the indirect partners?

A settlement agreement entered into by a pass-thru partner binds an indirect partner regarding the indirect partner's interest in the partnership held through the pass-thru partner, unless the indirect partner has been identified as provided in section 6223(c)(3). I.R.C. § 6224(c)(1); Treas. Reg. § 301.6224(c)-2(a). No additional language is necessary to bind the indirect partner. Id. The agreement binds the indirect partner regarding only partnership-level determinations; the indirect partner has not waived any other restriction on assessment or partner-level defenses. I.R.C. § 6224(c)(1). See IRM 8.19.3.9.2(5) and (6), *Who May Bind*; IRM 8.19.5.11(3), *Case Closings--Appeals Processing Services*.

Treas. Reg. § 301.6224(c)-2(b) identifies who may sign a settlement agreement on behalf of the pass-thru partner. If the entity is a limited liability company, then a manager of the LLC, under State law, must sign, regardless of whether the LLC is subject to the TEFRA partnership procedures.

4. Does the TMP have authority to bind all partners to a settlement agreement?

If the partnership has more than one hundred partners, and if the TMP enters into a settlement agreement expressly binding other partners, then that agreement binds any partner that: has less than a one percent interest in the profits of the partnership; is not part of a section 6223(b)(2) notice group; and has not filed with the Service a section 6224(c)(3)(B) statement that the TMP lacks such authority.[8] I.R.C. § 6224(c)(3). The agreement binds the nonnotice partner regarding only partnership-level determinations; the nonnotice partner has not waived any other restriction on assessment or partner-level defenses. I.R.C. §§ 6224(c)(1) and (3). See Treas. Reg. § 301.6224(c)-1(a); IRM 4.31.2.2.8(4), *Securing Agreements from the TMP and the Partners*.

5. If a partner is a member of a consolidated group, then who signs the settlement agreement?

If a partner is a member of a consolidated group, the identity of the persons who sign a settlement agreement depends on, at a minimum, the following variables: whether the partner is a parent or subsidiary corporation, whether the settlement agreement involves tax years beginning on or after June 28, 2002, and whether the partner is the TMP of the TEFRA partnership. See Treas. Reg. § 1.1502-77A(a) (for tax years beginning before June 28, 2002); Treas. Reg. §§ 1.1502- 7(a)(2)(iv), (a)(3)(v) and (a)(6)(iii) (for tax years beginning on or after June 28, 2002).

For identification of who must sign the settlement agreement for each combination of variables, see IRM 8.19.3.8.6(2)-(7), *Who Must Sign Agreements*.

[8] The signature must be that of the tax matters partner rather than that of the tax matters partner's counsel. I.R.C. § 6224(c)(3). See IRM 4.31.2.2.5(1)(a), *Power of Attorney Appointed by the Tax Matters Partner*.

6. Must the Service give the TMP notice of each settlement agreement?

Under Tax Court Rule 248(c), the Service must notify the TMP of all partner settlements occurring after the case has become docketed. The Service must serve on the TMP a statement identifying: the parties to the settlement; the date of the agreement; the year(s) to which the agreement relates; and the terms of the agreement as to each partnership item and the allocation of the partnership items among the partners. Within seven days of receiving that statement, the TMP must serve a copy of the statement upon all parties to the action. Tax Court Rule 248(c). The Service must also promptly file with the Tax Court a notice of settlement or consistent agreement with a participating party. Id. This affords the Tax Court and participating partners notice of which partners remain as participating partners under section 6226(d)(1)(A) and Tax Court Rule 247. The TMP forwards the settlement terms to the other partners allowing them to exercise their section 6224(c)(2) right to a consistent agreement. Tax Court Rule 248(c); Court of Federal Claims Appendix F, Rule 7; Monti v. Commissioner, 223 F.3d 76, 79-85 (2nd Cir. 2000). See Treas. Reg. § 301.6223(g)-1(b)(1)(iv). Section 6103(h)(4) authorizes the disclosure of information regarding settlements to the TMP because the settling partner was a party to the administrative or court proceeding and the remaining partners have a right to know of the settlement because of their right to a consistent agreement under section 6224(c)(2).

7. If a TMP is willing to settle adjustments to partnership items on behalf of the partnership, how does the Service close the section 6226 action?

Tax Court Rule 248(a) provides that a stipulation consenting to the entry of decision, executed by the TMP and filed with the Tax Court, binds all parties. See also Court of Federal Claims Appendix F, Rule 7. The signature of the TMP constitutes a certification by the TMP that no party objects to entry of decision.[9] Id. See CCDM Exhibit 35.11.1-188, *TEFRA: Rule 248(a) Decision per Settlement—Tabular Format-TEFRA Partnership*. As discussed above, all partners for the subject taxable year are parties except those who have already entered into settlement agreements or whose partnership items have otherwise converted, under section 6231(b)(1), into nonpartnership items. I.R.C. §§ 6226(c) and (d)(1)(A); Tax Court Rule 247. See IRM 8.19.3.14.3, *Settlement with Partners of Docketed TEFRA Entities*; CCDM 35.8.6.1.1(1), *Rule 248(a)—Decision Documents*.

8. If the Service enters into settlement agreements with all participating partners, then how does the Service close the section 6226 action?

Tax Court Rule 248(b) provides that if all participating partners (see Tax Court Rule 247(b)) have settled or do not object to entry of decision, then, after the expiration of the time within which to file a notice of election to intervene or to participate, the Service shall submit to the court a proposed decision document and motion for entry of decision. See also Court of Federal Claims Appendix F, Rule 7. Unlike a Tax Court Rule 248(a) decision, the TMP does not certify that no party objects when the Tax Court Rule 248(b) procedures are utilized.

The proposed decision must be in the form prescribed by Tax Court Rule 155 (*i.e.*, the proposed decision should not contain any stipulation or signature line for the parties, etc.). See CCDM 35.8.6.1.2(1), *Rule 248(b)—Decision Documents*. In addition, the certificate of service should reflect service on both the TMP and all participating partners. Tax Court Rule 246.

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[9] The signature must be that of the tax matters partner rather than that of the tax matters partner's counsel. See Tax Court Rule 248(a); and IRM 4.31.2.2.5(1)(b), *Power of Attorney Appointed by the Tax Matters Partner*. Typically, both sign.

Within three days from the date on which the Service files the motion for entry of decision, the Service must serve on the TMP a certificate showing the date on which the Service's motion was filed with the Tax Court. Tax Court Rule 248(b). That certificate is in addition to, and distinct from, the Tax Court Rule 246 certificate of service. Tax Court Rule 246. The Tax Court Rule 248(b) certificate may take any form (*e.g.*, a letter captioned "Certificate of Date of Filing") and is not filed with the Tax Court.

Within three days after receiving the Tax Court Rule 248(b) certificate, the TMP must serve upon all nonparticipating partners the Tax Court Rule 248(b) certificate, a copy of the motion, a copy of the proposed decision, and a copy of Tax Court Rule 248. Tax Court Rule 248(b). Any nonparticipating partner objecting to the Service's motion must file a motion for leave to participate. If, within sixty days from the date on which the Service filed its motion, no nonparticipating partner files a motion to participate, then the Tax Court may enter the proposed decision.

Please direct questions regarding this notice to Procedure and Administration Branch 6 at (202) 622-7950, or Branch 7 at (202) 622-4570. All cases with an overstatement of basis as an omission from gross income for purposes of the six-year period of limitations must be coordinated with the Office of the Associate Chief Counsel (Procedure and Administration).

/s/
Deborah A. Butler
Associate Chief Counsel
(Procedure and Administration)